A green light for Wall Street bailouts

US Senate moves towards passage of financial “reform” bill

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7 May 2010

By an overwhelming, bipartisan vote of 93-5 Wednesday, the US Senate removed the main obstacle to the passage of the misnamed “financial reform” legislation proposed by the Obama administration. The vote approved an amendment to the 1,400-page bill that is now before the Senate, scrapping a provision to tax the banks and use the proceeds to create a $50 billion fund to use in any future financial crisis.

The amendment was agreed on by Senator Christopher Dodd of Connecticut and Senator Richard Shelby of Alabama, the Democratic chairman and the ranking Republican of the Senate Finance Committee. It followed weeks of demagogy by the Republicans, claiming they opposed the measure because they wanted “no more bailouts” of the big banks.

It would be more accurate to say that neither party wants to impose any significant restriction on the financial manipulations and profit-gouging on Wall Street. The draft legislation, despite its size and purported scope, would neither punish those who caused the 2008 crash nor prevent future financial paroxysms. The intrinsic instability of the capitalist financial system was demonstrated only one day after the Senate vote, with Thursday’s 1,000-point plunge in the Dow Jones average in the space of five minutes.

The Dodd-Shelby amendment eliminated the proposed $50 billion fund, to be financed by a fee paid by all major banks to the US Treasury, in favor of a provision that would collect money from the banks after, rather than before, a major failure.

The bank-financed bailout fund had been initially opposed by the Obama administration, but was added to the legislation by Senate Democrats who wanted to posture as opponents of future bailouts funded by the Treasury. The measure was opposed by the big banks, since the fees to create the bailout fund would come out of their revenues. Senate Republicans followed the lead of the banks, while at the same time pretending that they were actually opposing a future taxpayer bailout.

Dodd claimed the change was not of major significance, declaring, “Because whether they pay in advance or after the fact these costs will be paid by Wall Street and not taxpayers.” But the change demonstrates the false pretenses at the core of the legislation.

In the event of a major bank failure, on the scale of the 2008 collapse of Lehman Brothers, the federal government will rush in as it did at that time, to save the financial aristocracy at the expense of the American people. The last thing the White House, Treasury or Federal Reserve would do under conditions of such a crisis of confidence is impose a new cost on the banks.

While both parties claim to oppose future bank bailouts, the Dodd-Shelby amendment lays out an explicit procedure under which the FDIC would use credit lines from the Treasury to finance the liquidation of a bank deemed “too big to fail.” The two senators claimed that these loans would be recovered through sell-off of the failed bank’s assets, but that is hardly likely under conditions of a major collapse in financial markets.

After passage of the Dodd-Shelby amendment, the Senate went even further in foreswearing future bailouts, with a 96-1 vote for a three-paragraph amendment by Sen. Barbara Boxer, a liberal Democrat from California, declaring that taxpayers would not bear any losses from the liquidation of bankrupt firms. This is roughly the equivalent of a confirmed alcoholic signing a sobriety pledge in between swigs of whiskey.

Far more significant than the rhetorical tub-thumping against bailouts of Wall Street is the fact that the Senate is adamantly opposed to any new taxes and fees on the financial institutions that less than two years ago triggered a worldwide financial crisis and the deepest slump since the Great Depression.

Wednesday's vote eliminated $50 billion in proposed fees on the banks. In addition, most senators are giving short shrift to the Obama administration's proposal for a tax on financial transactions that would raise $90 billion over a ten-year period to partially reimburse the Treasury for the cost of the Troubled Assets Relief Program (TARP), the original bank bailout.

While the substance of the bill has been largely shaped by banking industry lobbyists, several Senate Democrats have introduced amendments that would sharply curtail the financial manipulations of the biggest banks, one to limit the size of the banks (which predictably failed in a 33-61 vote Thursday evening) and the other to ban derivatives trading by banks.

These amendments are so much cynical play-acting, since the senators who introduced them know very well that the Democratic leadership and the Obama administration will not permit them to become law. They only want to posture as scourges of Wall Street to confuse public opinion, and in some cases, for immediate political gain. The ban on derivatives trading, for instance, was introduced by Blanche Lincoln of Arkansas, one of the most conservative Democrats in the Senate, who is facing a more liberal challenger in this month's primary.

Treasury Secretary Timothy Geithner, in congressional testimony Tuesday, suggested that the ban on derivatives trading by banks "will create a less stable system," since other institutions will become the primary traders of the exotic financial instruments, a market of staggering size, estimated at $294 trillion.

FDIC chairman Sheila Bair sent a letter to the Senate spelling out this argument, declaring, "If all derivatives market-making activities were moved outside of bank holding companies, most of the activity would no doubt continue, but in less regulated and more highly leveraged venues."

The real question is why derivatives trading—what billionaire Warren Buffett famously described as "financial weapons of mass destruction"—should be permitted at all. It is only the most noxious and notorious form of the parasitic speculation that is the sole purpose of Wall Street.

In response to pressure from bank lobbyists and the White House, several leading Democrats in the Senate indicated they would back off the restrictions on derivatives. Lincoln herself said Wednesday that banks would be allowed to spin off their derivatives trading to affiliates, essentially preserving the existing setup with a change in labels.